

# **FARM POLICY**

***UPDATE***

***SHORTCOMINGS***

***ALTERNATIVES***

**Presented**

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**To**

**National Agricultural Credit Meeting**

**Chicago FED**

**September 13, 1999**

# UPDATE

**Nothing Changed ---- No Update  
(yet)**

## REVIEW

### **FAIR Act Ended**

*Set Asides  
Government Stocks  
Coupled Payments  
Large EEP Payments*

### **FAIR Act Enabled Farmers to**

*Plant Without Restriction  
Respond to the Market  
Hang Themselves*

**FAIR Act "Tried" to**

***End Disaster Programs***

***Shift Responsibility for Risk to Operators***

***Enable and Encourage Use of Crop Insurance***

***Provide Money for Transition Difficulties***

# SHORTCOMINGS

## Loan Rates Too High

*Failure to Recognize Production will continue in the Short Run so Long as Price Exceeds Variable Cost of Production*

Crop	Variable Cost	Loan Rate
Corn	\$1.25	\$1.89
Soybean	\$2.50	\$5.26
Wheat	\$2.15	\$2.58

## **Loan Rates and Cost of Production Not Balanced**

***In a Low Price Scenario the Loan/Cost Ratio and Unlimited LDP Encourages Oilseed Production***

<b>Crop</b>	<b>Yield</b>	<b>Price</b>	<b>Net Per Acre</b>
<b>Corn</b>	<b>140</b>	<b>\$1.90</b>	<b>\$ - 10</b>
<b>Soy</b>	<b>45</b>	<b>\$4.75</b>	<b>\$ 125</b>

## **Freedom to Plant Allowed Shift in Acres**

***Farmers Shifted Wheat Acreage to Soybeans***

<b>Crop</b>	<b>Million Acres Planted</b>	
	<b>1996</b>	<b>1999</b>
<b>Wheat</b>	<b>75.6</b>	<b>64.3</b>
<b>Soybean</b>	<b>64.3</b>	<b>74.1</b>

## **Failed to Fix Crop Insurance**

***Producers Remain Reluctant to Purchase as a  
Primary Risk Management Tool***

## **Unable to Restrain Congress in Face of Disaster**

***Congress Rushes in With Aid in 1998 and 1999  
Even Though Farmers Were Told  
"No More Disaster Programs"***

***Farmers Don't Learn to Manage Risk in This  
Kind of Political Environment***

## **Front-Loading of AMTA Payments**

***'96 and '97 AMTA Payments Made on Top of  
High Prices Encouraging Increased Production  
and Higher Land Costs***

**Unable to Control Macro and Global  
Economy and Politics**

***Stronger Dollar***

***Commodity Deflation***

***Asian Financial Crisis***

***Unexpected Barriers to Trade***

***Weak Response to Trade Barriers***

***"Domestic and Foreign Monetary, Fiscal and  
Political Policies Can Swamped Farm Policy"***

# ALTERNATIVES FOR THE FUTURE

## Ten Key Propositions

1. *Global food supply-demand more favorable in future*
2. *Principal economic problem of farmers will be instability*
3. *Markets for farm commodities work*
4. *Farms will become*  
*Larger*  
*More high tech*  
*More industrialized*  
*More challenging to manage / finance*
5. *Most farms will be family farms and will deal with fewer and larger suppliers and buyers*



6. *Non-commercial farms will decline in number and output*
7. *Cash flow will continue to threaten farms*
8. *Government transfer payments to farmers likely to continue*
9. *Pressure for regulation will increase*
10. *Farm exports will expand at uneven rate*

## **Policy Alternatives**

**WTO Illegal (blue box) or Rejected by Congress**

***Supply Management***

***Price Supports Above Cost of Production***

***Dumping Commodities***

***Government Stock Accumulation***

## WTO Legal (green box)

*Research, Education, Extension, Information  
Grades and Standards*

*Exports*

*Promotion*

*Low Interest Loans and Guarantees*

*Food Aid*

*Environmental Protection*

*CRP*

*EQUIP*

*Wetlands Reserve*

*Technical Assistance*

*Infrastructure Investment*

*Ports*

*Rails*

*Roads*

*...*

*Sanitary - Phytosanitary science restrictions*

*Fair Act*

*Production Flexibility Contract Payments*

*Loan Rates - if set low enough*

*Disaster Assistance*

*Insurance Programs*

## **Worthy of Consideration (amber box)**

### ***U.S. Concerns with Foreign Policies***

***Supply Management (Canada)***

***Export Subsidies (EU)***

***Minimum Access and High Tariffs (Japan)***

***State Trading Companies (Japan)***

***SPS used for Protection (EU)***

### ***Foreign Concerns about U.S.***

***Loan Price Above World Price***

***Direct Payments (coupled)***

***Per Animal***

***Tied to Production***

***Subsidy component***

***Insurance***

***Disaster Assistance***

***Loan Rates***

***Export Assistance***

## Options Being Considered

### *Insurance*

*Farmers Are Not Risk Averse*

*High subsidy has WTO problem (coupled)*

*Encourages production in marginal areas*

*Excess production reduces prices for all*

*What to cover?*

*Yield*

*Price*

*Revenue*

*Costs*

*Net farm income*

*Net family income*

*Farmers Face Bewildering Set of Choices*

*Multiple Peril*

*Crop Revenue Coverage*

*(tied to futures price)*

*Revenue Insurance*

*(tied futures adjusted to local)*

***Income Protection***  
***(tied to February prices)***

***Adjusted Gross Income***  
***(multiple commodities)***

***Net Income (experimental)***  
***(like a "matched" IRA)***

***Advantages***

***Targets net income***  
***Cost effective***  
***Easy to administer***

***Disadvantages***

***No income - No subsidy***  
***Run of bad years problem***  
***No advance payments***  
***Beginning farmer problem***  
***Omits off-farm income***

## ***Raise Loan Rates***

***Increases production***

***Lowers price***

***Increase LDP***

***Encourages marketing during glut***

***Higher cost to taxpayer***

## ***Increase CRP***

***Reduces U.S. production***

***Raises world price***

***Encourages foreign production***

## ***Flexible Fallow (Harkin)***

<b>Set-Aside Rate (%)</b>	<b>Loan Rate</b>		
	<b>Corn</b>	<b>Wheat</b>	<b>Soybean</b>
<b>0</b>	<b>\$1.89</b>	<b>\$2.75</b>	<b>\$4.72</b>
<b>10</b>	<b>2.09</b>	<b>3.04</b>	<b>5.21</b>
<b>20</b>	<b>2.41</b>	<b>3.51</b>	<b>5.96</b>
<b>30</b>	<b>2.75</b>	<b>4.01</b>	<b>6.76</b>

# **CONCLUDING COMMENTS**

**Technological Treadmill Will Continue**

**Competent Managers Will Earn Adequate Income  
With or Without Government Programs**

**Problems of Risk, Environment, Cash Flow,  
Adjustment to Vertical Integration and  
Economies of Size Will not Go Away**

**Addressing These Problems Begins With Private  
Markets and "Green Box" activities**

**Raising Loans Has Serious Problems**

**FUTURE Policy Might Well Consider Net Farm  
or Family Net Income**

**If Transfers are Essential, Consider**

**Continue De-coupling  
Payments for Soil Conservation  
Payments for Water Quality  
Payments for Air Quality  
Payments for Carbon Sequestration**